

Number: **200818003**
Release Date: 5/2/2008
Index Number: 2055.12-10

Third Party Communication: None
Date of Communication: Not Applicable

Telephone Number:

Refer Reply To:
CC:PSI:B4
PLR-105774-07
Date:
January 28, 2008

Decedent	=
Trust	=
State	=
Date 1	=
\$ <u>a</u>	=
\$ <u>b</u>	=
Child 1	=
Child 2	=
Grandchild 1	=
Grandchild 2	=
Grandchild 3	=
\$c	=

This is in response to your letter, dated January 29, 2007, in which you requested rulings regarding the proposed reformation of a trust into a charitable remainder unitrust (CRUT).

Article II of Trust provides that the net income of the trust shall be accumulated by the trustee for a period of approximately five years. Beginning on Date 1, the trustee is directed to pay to Wife the sum of \$a per month during her life. Twelve months after Wife's death, the trustee is directed to distribute out of the income of the trust estate the sum of \$b per month to each of Child 1 and Child 2 during their respective lifetimes. Twelve months after the death of Child 1, the trust provides for the payment of \$b per month, to be divided equally among the children of Child 1. Twelve months after the

death of Child 2, the trust provides for the payment of \$b per month, to be divided equally among the children of Child 2.

Article IV provides that the income of the trust shall not be accumulated for any period longer than twenty-one years after the death of Decedent, at the end of which all of the income from the trust shall be distributed to the beneficiaries then entitled to any portion or portions of the income.

Article V provides the rule against perpetuities provision.

Article VI provides, in part, that upon the death of the last survivor of Wife, Child 1, Child 2, and the children of Child 1 and Child 2, the principal and income then remaining shall be retained by the trustee, and thereafter the trustee shall distribute the net trust income to whomever it may select, for the purpose of the correction or betterment of crippled or underprivileged children under the age of twenty-one, for the purpose of enabling them to become able in mind, and to provide artificial limbs, medical, surgical, and hospital care.

Decedent died on _____, 1954. As a result, Trust converted from fixed dollar payments of income to the payment of all net income at the end of twenty-one years after Decedent's death.

Wife, Child 1, and Child 2 are now deceased. The current income beneficiaries are Grandchild 1, Grandchild 2, and Grandchild 3, the sole surviving children of Child 1 and Child 2. The current value of Trust is approximately \$c.

On June 6, 2006, the trustee petitioned the local court to reform Trust to "establish" a charitable remainder trust within the meaning of Rev. Proc. 2005-55, 2005-2 C.B. 367 and § 664(d)(2) of the Internal Revenue Code. The same day, the local court entered an order to reform Trust. The order deemed the reformation effective as of January 1, 2006.

As reformed, Trust provides, among other things, that, in each taxable year of the trust during the unitrust period, the trustee shall pay to Grandchild 1, Grandchild 2, and Grandchild 3, in equal shares during their joint lives, a unitrust amount equal to five percent of net fair market value of the assets of the trust valued as the first day of each taxable year of the trust. Upon the death of any recipient, the trustee shall pay the entire amount to the survivors or survivor. The first day of the trust shall be January 1, 2006, and the last day of the unitrust period shall be the date of the final survivor recipient's death. The unitrust amount shall be paid in equal monthly installments "on or about" the fifteenth day of each month from income, and to the extent income is not sufficient, from principal.

The trustee has requested a ruling that Trust, as reformed, qualifies as a charitable remainder unitrust under § 664(d)(2) of the Internal Revenue Code.

Pursuant to § 4.01(37) of Rev. Proc. 2007-3, 2007-1 I.R.B. at 114, the Internal Revenue Service (Service) ordinarily will not issue rulings as to whether a charitable remainder trust that provides for annuity or unitrust payments for one or two measuring lives satisfies the requirements described in § 664. In lieu of seeking the Service's advance approval of a CRUT, taxpayers are directed to follow the sample CRUT provisions outlined in Rev. Proc. 2005-55, 2005-2 C.B. 367. By following the model contained in Rev. Proc. 2005-55, taxpayers can be assured that the Service will recognize a trust as meeting all of the requirements of a qualified CRUT under § 664(d)(2), provided that the trust operates in a manner that is consistent with the terms of the trust instrument and that the trust is a valid trust under applicable local law. The issue raised in the ruling request is not directly addressed in Rev. Proc. 2005-55. Therefore, we will rule on whether Trust, as reformed, qualifies as a CRUT under § 664(d)(2).

Section 664(d)(2) provides, in relevant part, that a CRUT is a trust: (A) from which a fixed percentage (which is not less than 5 percent nor more than 50 percent of the initial net fair market value of all property placed in trust) is to be paid, not less frequently than annually, to one or more persons (at least one of which is not an organization described in § 170 and, in the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not in excess of 20 years) or for the life or lives of such individual or individuals; (B) from which no amount other than the payments described in § 664(d)(2)(A) and other than qualified gratuitous transfers described in § 664(d)(2)(C) may be paid to or for the use of any person other than an organization described in § 170(c); (C) following the termination of the payments described in § 664(d)(2)(A), the remainder interest in the trust is to be transferred to, or for the use of, an organization described in § 170(c) or is to be retained by the trust for such a use; and (D) with respect to each contribution of property to the trust, the value (determined under § 7520) of such remainder interest in such property is at least 10 percent of the net fair market value of such property as of the date such property is contributed to the trust.

Section 2501(a)(1) imposes a tax, for each calendar year, on the transfer of property by gift by any individual, resident or nonresident.

Section 2522(a)(2) provides, in part, that in computing taxable gifts for the calendar year, there shall be allowed as a deduction the amount of all gifts made during such year to or for the use of a corporation, or trust, or community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 2522(c)(2) disallows the gift tax charitable deduction where a donor transfers an interest in property (other than an interest described in § 170(f)(3)(B)) to a person, or for a use, described in § 2522(a), and an interest in the same property is retained by the donor, or is transferred or has been transferred (for less than an adequate and full consideration in money or money's worth) from the donor to a person, or for a use, not described in § 2522(a), unless --(A) in the case of a remainder interest, such interest is in a trust which is a charitable remainder annuity trust or a charitable remainder unitrust (described in § 664) or a pooled income fund (described in § 642(c)(5)), or (B) in the case of any other interest, such interest is in the form of a guaranteed annuity or is a fixed percentage distributed yearly of the fair market value of the property (to be determined yearly).

Section 2522(c)(4)(A) provides that a deduction is allowed under § 2522(a) in respect of any qualified reformation (within the meaning of § 2055(e)(3)(B)). Section 2522(c)(4)(B) provides that for purposes of § 2522(c), rules similar to the rules of § 2055(e)(3) shall apply. Section 2055(e)(3)(A) provides that a deduction shall be allowed under § 2055(a) in respect to a qualified reformation.

Prior to the Tax Reform Act of 1969 (the Act), there were no substantial restrictions on estate or gift tax charitable deductions for income and remainder interests that passed to charities. The Act added §§ 664, 2055(e), and 2522(c) to the Code. Under § 2055(e), no estate tax deduction is allowed for certain remainder interests passing to charity unless the interest is in the form of a charitable remainder trust described in § 664 or a pooled income fund described in § 642(c)(5). Section 201(d)(1) of the Act, Pub. L. No. 91-172, 83 Stat. 560. Similarly, under § 2522(c), no gift tax deduction is allowed for certain remainder interests passing to charity unless the interest is in the form of a charitable remainder trust described in § 664 or a pooled income fund described in § 642(c)(5). Section 201(d)(3) of the Act. The Act applies generally to decedents who died after December 31, 1969, or to gifts made after July 31, 1969. Section 201(g) of the Act.

In 1974, § 2055(e)(3) was added to the Code. Section 2055(e)(3) permitted a post-death reformation of a trust to qualify under § 2055(e)(2) and thus, qualify for the estate tax charitable deduction under § 2055(a). This amendment allowing post-death reformations applies only to estates of decedents dying after December 31, 1969. Pub. L. No. 93-483, 88 Stat. 1457.

Congress added § 2522(c)(4) to the Code in the Tax Reform Act of 1984, which permits an inter vivos split interest trust to be reformed to qualify for the gift tax charitable deduction under § 2522(a). Section 1022, 98 Stat. 1026. To qualify for the deduction, the trust must be reformed in a manner similar to rules provided in § 2055(e)(3).

In this case, the trustee of Trust obtained an order from the local court approving the reformation of Trust into a trust that will satisfy the requirements under § 664. Generally, in order for a trust to be a charitable remainder trust, it must meet the definition and function exclusively as a charitable remainder trust from the creation of the trust. Section 1.664-1(a)(4). Trust has not functioned exclusively as a charitable remainder trust since its inception.

In limited circumstances, a trust may be reformed to qualify as a charitable remainder trust. With respect to inter vivos transfers, § 2522(c) permits a trust to be reformed to qualify for the gift tax charitable deduction under § 2522(a) (i.e., the trust will meet the requirements of § 664(d)(1) or (2)). The trust must be reformed in a manner consistent with rules provided in § 2055(e)(3). The reformation provision that allows a remainder interest in a split interest trust to qualify for the gift tax charitable deduction applies only to transfers made after 1969. In this case, the transfer took place in 1954. Therefore, we conclude that Trust, as reformed, will not qualify as a valid charitable remainder trust under § 664(d) for Federal income, gift or estate tax purposes.

This ruling is directed only to the taxpayers requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

The rulings contained in this letter are based upon information and representations submitted by the taxpayers and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

James F. Hogan
Senior Technician Reviewer, Branch 9
(Passthroughs & Special Industries)